



STATE BOARD OF EQUALIZATION

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MICHELLE STEEL
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Fourth District, Los Angeles

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State Controller

KRISTINE CAZADD
Interim Executive Director

March 3, 2011

Dear Stakeholder:

Enclosed are two legislative proposals Board staff is considering for the current legislative session. These proposals have not yet been approved by the Board Members. The proposals may be presented for consideration at a future Board of Equalization Legislative Committee meeting. However, before the proposals are presented at the Legislative Committee meeting, staff would like to provide stakeholders an opportunity to discuss the issues and present any suggested changes or comments. Accordingly, a meeting is scheduled in **Room 122 at 10:00 A.M. on March 16, 2011**, at the Board of Equalization; 450 N Street; Sacramento, California.

If you are unable to attend the meeting but would like to provide input for discussion at the meeting, please feel free to write to me at the above address or send a fax to (916) 322-4530 before the March 16, 2011 meeting. If you are aware of other persons that may be interested in attending the meeting or presenting their comments, please feel free to provide them with a copy of the enclosed material and extend an invitation to the meeting. If you plan to attend the meeting on March 16, 2011, or would like to participate via teleconference, I would appreciate it if you would let staff know by contacting Mr. Bradley Miller at (916) 319-9924 or by e-mail at Brad.Miller@boe.ca.gov prior to March 14, 2011. This will allow staff to make alternative arrangements should the expected attendance exceed the maximum capacity of Room 122 and to arrange for teleconferencing.

Whether or not you are able to attend the above stakeholders' meeting, please keep in mind that the due date for stakeholders to provide written comments regarding the legislative proposal is **March 24, 2011**. Please be aware that a copy of the material you submit may be provided to other stakeholders. Therefore, please ensure your comments do not contain confidential information.

Thank you for your consideration.

Sincerely,

Susanne Buehler
Chief, Tax Policy Division
Sales and Use Tax Department

SB: BEM

Enclosures

cc: (all with enclosures)

Honorable Jerome E. Horton, Chairman, Fourth District
Honorable Michelle Steel, Vice Chair, Third District
Honorable Betty T. Yee, Member, First District (MIC 71)
Senator George Runner (Ret.), Member, Second District (MIC 78)
Honorable John Chiang, State Controller, c/o Ms. Marcy Jo Mandel

(Via E-mail)

Ms. Shellie Hughes, Board Member's Office, Fourth District
Mr. Robert Thomas, Board Member's Office, Fourth District
Mr. Neil Shah, Board Member's Office, Third District
Mr. Tim Treichelt, Board Member's Office, Third District
Mr. Alan LoFaso, Board Member's Office, First District
Ms. Mengjun He, Board Member's Office, First District
Mr. Lee Williams, Board Member's Office, Second District
Ms. Natasha Ralston Ratcliff, State Controller's Office
Ms. Kristine Cazadd
Mr. Randy Ferris
Ms. Margaret Shedd
Mr. Jeffrey L. McGuire
Ms. Christine Bisauta
Mr. Robert Tucker
Ms. Sandy Barrow
Mr. Kevin Beile
Ms. Sheila Waters
Ms. Trista Gonzalez

Ms. Aimee Simons
Mr. Lou Feletto
Mr. Geoffrey E. Lyle
Ms. Leila Hellmuth
Bradley Miller

Proposal #1

Add section 6092.5 to the Revenue and Taxation Code to provide that every person selling a vehicle at auction may not accept a resale certificate from a purchaser who is not a licensed dealer or dismantler.

Source: Deputy Director's Office – SUTD

Existing Law

Revenue and Taxation Code (RTC) section 6272 provides that the term “vehicle” is as defined in section 670 of the Vehicle Code and shall include off-highway motor vehicles subject to identification under Division 16.5 (commencing with section 38000) of the Vehicle Code. RTC section 6275 provides that every person making any retail sale of a vehicle required to be registered under the Vehicle Code or subject to identification under Division 16.5 of the Vehicle Code, is a retailer of the vehicle for the purposes of the Sales and Use Tax Law regardless of whether he or she is a retailer by reason of any other provision of the Sales and Use Tax Law. RTC section 6282 exempts from the sales tax the gross receipts from the sales of vehicles required to be registered under the Vehicle Code when the retailer is other than a person licensed under the Vehicle Code as a manufacturer, remanufacturer, dealer, dismantler, or lessor-retailer, subject to Vehicle Code section 11615.5 of the Vehicle Code. RTC section 6292 provides that when a vehicle is sold at retail by other than a person licensed under the Vehicle Code as a manufacturer, remanufacturer, dealer, dismantler, or lessor-retailer, the retailer is not required or authorized to collect the use tax from the purchaser, but the purchaser of the vehicle shall pay the use tax to the Department of Motor Vehicles (DMV).

These sections provide that every person making a retail sale of a vehicle is a retailer, but the retailer is exempt from the sales tax when the retailer is not a licensed dealer with DMV. In this instance, the applicable tax is a use tax rather than a sales tax. The purchaser of the vehicle is required to pay the use tax to the DMV at the time of registration.

Chapter 3 of Division 5 of the Vehicle Code, commencing with section 11500 provides for the requirements of a person wishing to engage in business as an automobile dismantler. The law requires such a person to have a permanent place of business and to apply for a dismantler's license with the DMV.

This Proposal

This proposal would provide that any person selling a vehicle may not accept a resale certificate from a purchaser who is not a licensed dealer. For the purposes of this proposal, a licensed dealer includes a person licensed as a dismantler with DMV. The sale of a vehicle to a person other than a licensed dealer is a retail sale and the seller is liable for the sales tax.

Background

The sales tax is generally imposed upon the retailer for the privilege of selling tangible personal property at retail in this state. If a person is purchasing property for the purpose

of reselling the property prior to any use of the property, the seller may accept a resale certificate from the purchaser. Acceptance of a resale certificate in good faith relieves the seller of the liability for the sales tax. The purchaser is then liable for the sales tax on the subsequent retail sale of the property (unless the property is again sold for resale or is exempt for some other reason).

The same provisions generally apply to sales of vehicles. However, persons engaged in the business of selling vehicles are generally required by the Vehicle Code to obtain a license to sell vehicles from the DMV. This license is generally referred to as a dealer's license. Persons engaged in the business of auto dismantling must obtain a dismantler's license from DMV. Sales of vehicles for resale between licensed dealers and dismantlers are generally permitted and require the issuance and acceptance in good faith of a resale certificate.

The sale of a vehicle by a non-dealer is still a retail sale. These are generally referred to as private party sales. A private party seller may or may not have a seller's permit. In a private party sale, the non-dealer seller is not liable for the sales tax on the sale of the vehicle, even if the seller has a seller's permit. Instead, the purchaser is liable for use tax. The purchaser pays the use tax to the DMV at the time of registration. Both the purchaser and private party seller complete necessary forms notifying the DMV of the vehicle sale.

The problem area involves salvage certificate vehicles. A salvage certificate vehicle is a vehicle that has been wrecked or damaged, and the owner, insurance company, financial institution or leasing company considers it too expensive to repair. Generally, this involves forwarding the certificate of ownership, license plates, and a required fee to the DMV. The DMV then issues a salvage certificate for the vehicle. The vehicle may subsequently be repaired and re-registered with the DMV. To be re-registered, the vehicle must pass a safety inspection with the DMV or the California Highway Patrol. It is then classified as a "revived salvage" or "salvaged" vehicle.

Since a salvage certificate vehicle is not subject to registration with DMV, an auto auction selling such a vehicle may currently accept a resale certificate from any person with a seller's permit, not just a licensed dealer. For example, a person with a seller's permit for the operation of a restaurant may properly issue a resale certificate for the purchase of a salvage certificate vehicle from an auto auction if the salvage certificate vehicle will be resold by the purchaser. The purchaser may resell the salvage certificate vehicle as-is, sell the various parts and components of the vehicle to different people, or repair the vehicle so that it may be resold as a vehicle that may be operated on the highway again.

This proposal is intended to close a tax gap in the auto auction industry that allows non-dealers to purchase vehicles without tax by issuing a resale certificate at the time of purchase at a salvage auto auction. This proposal would require salvage auto auctions to collect tax on the sale of any vehicle that is sold to a non-dealer. Based on data received from auto auctions, a substantial number of vehicles are being purchased by non-dealers at salvage auto auctions.

Audits and investigations have disclosed permit holders that are not licensed dealers are acquiring salvage certificate vehicles by issuing a resale certificate, and are not reporting any subsequent sales of vehicles. Additionally, purchasers do not appear to be registering the vehicles with DMV and reporting use tax.

In addition to addressing the tax gap for vehicles sold at auction, this proposal may also provide consumer and environmental benefits. Requiring a person who is not a licensed dealer or dismantler to pay tax on the purchase of a salvage certificate vehicle at auction will act as an economic deterrent and may limit sales to these unlicensed purchasers. When a person who is not a licensed dealer or dismantler purchases a salvage certificate vehicle, there is a very good possibility that substandard repairs will be made to the vehicle before it is resold. This may result in an un-safe vehicle being sold to a consumer that may not realize the extent to which the vehicle was damaged previously. Also, licensed dismantlers are required to properly dispose of hazardous materials such as motor oil, anti-freeze, and refrigerant in a manner which protects the environment. An unlicensed person is not subject to the same requirements and inspections which results in unsafe disposal of these toxic materials.

To remedy this situation, the RTC should be amended to provide that any person selling a vehicle at auction may only accept a resale certificate from a person holding a dealer's license issued by DMV. Any sale of a vehicle at auction to a purchaser that does not hold a valid dealer's license issued by DMV is a retail sale and the retailer is liable for either the sales or use tax.

Section 6092.5 is added to the Revenue and Taxation Code to read as follows:

6092.5. Every person making any sale at auction of a mobilehome or commercial coach required to be registered annually under the Health and Safety Code, or of a vehicle required to be registered under the Vehicle Code or subject to identification under Division 16.5 (commencing with Section 38000) of the Vehicle Code, or a vehicle that qualifies under the permanent trailer identification plate program pursuant to subdivision (a) of Section 5014.1 of the Vehicle Code, or of any salvage certificate vehicle as defined in section 11515 of the Vehicle Code, is presumed to be making a sale at retail and not a sale for resale. The presumption may be rebutted by taking a resale certificate from a person who is licensed or certificated under the Health and Safety Code or the Vehicle Code as a dealer or dismantler. A person shall not accept a resale certificate from any person who is not licensed or certificated under the Health and Safety Code or the Vehicle Code as a dealer or dismantler.

Proposal #2

Add Article 1.2 to Chapter 8 of Part 1 of Division 2 of the Revenue and Taxation Code to require wholesalers and distributors of beer, wine, distilled spirits, cigarettes, and tobacco products to file quarterly electronic reports of sales amounts to retailers.

Source: Tax Policy Division

Existing Law

Revenue and Taxation Code (RTC) section 7054 provides that the Board of Equalization (BOE) may examine the books and records of any person selling tangible personal property in order to verify the accuracy of any return made.

Fuel wholesalers and suppliers are required to collect prepaid sales tax on wholesale transactions of motor vehicle fuel, aircraft jet fuel, and diesel fuel. Fuel wholesalers and suppliers are also required to file with the BOE a report providing sales information broken down by purchaser. Other than fuel wholesaler and suppliers, current law does not require the collection of prepaid tax or the filing of information returns for any other type of tangible personal property sold in this state.

This Proposal

This proposal would require suppliers and wholesalers of beer, wine, distilled spirits, cigarettes, and tobacco products to file sales reports electronically on a regular reporting basis (generally monthly or quarterly). This information could then be used for data matching with sales amounts reported by retailers to help identify reporting errors.

Background

Some states, such as Vermont and Washington, operate as monopoly states for the distribution of distilled spirits, beer, wine, cigarettes, or tobacco products. In these states, a state agency acts as the wholesaler of some or all of these products. Since the state is the person selling to the retailer, the sales amounts of each type of product to each retailer is known to the state.

Other states, such as Texas, New York, Illinois, and Iowa, require wholesalers to file reports with the state identifying how much of each type of product was sold to a retailer. These reports generally require the information be broken down by type of product sold and to whom it was sold. At the same time the report is filed with the state, some states also require the wholesaler to provide the retailer a summary report listing the sales amount to that retailer.

States that possess information about sales to retailer's, either due to information reporting by wholesalers or because the state was the wholesaler, are able to use this information to determine if retailers are reporting accurate sales amounts. If the state has information regarding how much of a certain product was sold to a retailer, the state can look at the reported retail sales by that retailer and determine very quickly if the reported sales are generally accurate. For example, if all wholesaler reports indicate Retailer A purchased \$10,000 worth of taxable products, but Retailer A only reported \$9,000 in taxable sales, it is very likely Retailer A has under reported taxable sales for the period.

Such a proposal can greatly increase tax compliance for two reasons. First, the BOE will be able to very quickly and easily determine which retailers are under reporting taxable sales by data matching the information provided. Second, if the retailer is aware the wholesaler is reporting specific figures to the state for use in evaluating compliance by the retailer, the retailer will be more likely to take steps to be self compliant for reporting taxable sales.

Pursuant to RTC section 7054, the BOE already has the authority to obtain sales information from distributors and wholesalers. This information is generally examined as part of an audit of a distributor or wholesaler. Additionally, BOE audit staff routinely request this information on an as-needed basis when conducting an audit of a person purchasing property for resale from the distributor or wholesaler when the records of the purchaser are missing or are deemed inadequate.

Requiring wholesalers and distributors to file sales reports in an electronic format with the BOE on a regular basis (monthly or quarterly) will provide the BOE with a more efficient way to manage data that the BOE already has the ability to obtain via other means. The information will allow for increased efficiencies in the audit program due to the ability to utilize a more efficient desk audit program and a more accurate audit selection program.

Imposing an additional reporting requirement on wholesalers and distributors of beer, wine, distilled spirits, cigarettes and tobacco products may be viewed by some as imposing an additional reporting burden on business. However, it may also alleviate wholesalers and distributor's current burden of responding to individual requests from BOE staff throughout the year. Additionally, wholesalers and distributors of these products already summarize sales figures by customer for marketing purposes or for reporting this information to other states. This proposal would simply require that the data be reported to the BOE electronically.

To ensure compliance with the proposed reporting requirement, a penalty in an amount of \$500 shall be imposed upon any wholesaler or distributor who fails to file the necessary report on a timely basis. However, since the BOE is more concerned about obtaining the necessary information from the reports filed by wholesalers and distributors, any penalties imposed by the BOE for failure to file the necessary report shall be refunded to the wholesaler or distributor at the time when the wholesaler or distributor files the delinquent report. The proposed statutes also clarify that failure to file such reports would not be grounds for revocation of a seller's permit held by a wholesaler or distributor.

Article 1.2, commencing with section 7061, is added to Chapter 8 of Part 1 of Division 2 of the Revenue and Taxation Code to read as follows:

Article 1.2. Reports by Wholesalers and Distributors of Beer, Wine, Distilled Spirits, Cigarettes, and Tobacco Products.

7061. For the purposes of this article, the following terms are defined as follows:

(a) "Beer" has the same meaning as provided in Business and Professions Code section 23006.

(b) "Cigarettes" has the same meaning as provided in section 30003.

(c) "Distilled Spirits" has the same meaning as provided in Business and Professions Code section 23005.

(d) "Distributor" means and includes a person defined as a distributor pursuant to section 30011 or a person who makes sales for resale to a retailer of beer, wine, distilled spirits, cigarettes, and tobacco products.

(e) "Retailer" means and includes any person defined as a retailer pursuant to section 6015 or Business and Professions Code section 23032.

(f) "Tobacco Products" has the same meaning as provided in section 30121.

(g) "Wholesaler" means and includes any person defined as a wholesaler pursuant to section 30016 or Business and Professions Code section 23021, or a person who makes sales for resale to a retailer of beer, wine, distilled spirits, cigarettes, and tobacco products.

(h) "Wine" has the same meaning as provided in Business and Professions Code section 23007.

7062. (a) The board, when considered necessary for the proper administration of this part, may require every person acting as a wholesaler or distributor of beer, wine or distilled spirits to file a report in an electronic format as prescribed by the board, of sales to retailers in this state.

(b) On or before the last day of the month following the reporting period, the wholesaler or distributor shall file a report with the board containing all of the following information:

(1) The name and address of the retail location to which the wholesaler or distributor delivered beer, wine, or distilled spirits.

(2) The seller's permit number of the retailer to which beer, wine, or distilled spirits were sold.

(3) The net sales amount by the wholesaler or distributor to the retailer for the reporting period, including quantities of units of beer, wine, and distilled spirits.

(c) For purposes of this section, a reporting period shall consist of a calendar quarter. However, in the event the board determines that a reporting period other than a calendar quarter would simplify reporting by distributors and wholesalers based on a written request by a distributor or wholesaler, the board may authorize an alternative reporting period.

(d) Any person who fails to file a report as required in this section shall pay a penalty of five hundred dollars (\$500) for each report that is not filed by the due date. That person shall be relieved of the penalty imposed for failure to timely file a report as required in this section at such a time when the person files the necessary report. Notwithstanding the provisions of section 6070, failure to file a report as required by this section shall not be grounds for revocation of a seller's permit.

(e) Information contained in reports filed with the board under this section shall constitute confidential taxpayer information pursuant to section 7056.

7064. (a) The board, when considered necessary for the proper administration of this part, may require every person acting as a wholesaler or distributor of cigarettes or tobacco products to file a report in an electronic format as prescribed by the board, of sales to retailers in this state.

(b) On or before the last day of the month following the reporting period, the wholesaler or distributor shall file a report with the board containing all of the following information:

(1) The name and address of the retail location to which the wholesaler or distributor delivered cigarettes or tobacco products.

(2) The seller's permit number of the retailer to which cigarettes or tobacco products were sold.

(3) The net sales amount by the wholesaler or distributor to the retailer for the reporting period, including quantities of units of cigarettes and tobacco products.

(c) For purposes of this section, a reporting period shall consist of a calendar quarter. However, in the event the board determines that a reporting period other than a calendar quarter would simplify reporting by distributors and wholesalers based on a written request by a distributor or wholesaler, the board may authorize an alternative reporting period.

(d) Any person who fails to file a report as required in this section shall pay a penalty of five hundred dollars (\$500) for each report that is not filed by the due date. That person shall be relieved of the penalty imposed for failure to timely file a report as required in this section at such a time when the person files the necessary report. Notwithstanding the provisions of section 6070, failure to file a report as required by this section shall not be grounds for revocation of a seller's permit.

(e) Information contained in reports filed with the board under this section shall constitute confidential taxpayer information pursuant to section 7056.